

THE NEIGHBORHOOD SHOPPING CENTER MARKET IN CALIFORNIA

by

Keith M. Gilbert

B.A., Yale University (1984)

Submitted to the Department of Urban Studies and Planning  
and the  
Center for Real Estate Development  
in Partial Fulfillment of the Requirements for the Degree of  
Master of Science in Real Estate Development

at the

Massachusetts Institute of Technology

August 1990

© Keith M. Gilbert 1990

The author hereby grants to MIT permission to reproduce and to  
distribute copies of this thesis document in whole or in part.

Signature of the Author \_\_\_\_\_  
Keith M. Gilbert  
Department of Urban Studies and Planning  
July 30, 1990

Certified by \_\_\_\_\_  
James McKellar  
Senior Lecturer, Department of Architecture  
Thesis Supervisor

Accepted by \_\_\_\_\_  
Gloria Schuck  
Chairperson

Interdepartmental Degree Program in Real Estate Development

MASSACHUSETTS INSTITUTE  
OF TECHNOLOGY

SEP 19 1990

**The Neighborhood Shopping Center Market in California**  
**by**  
**Keith M. Gilbert**

Submitted to the Department of Urban Studies and Planning and  
the Center for Real Estate Development in Partial Fulfillment of the  
Requirements for the Degree of Master of Science in Real Estate  
Development

**Abstract**

This paper attempts to provide an overview of the market that exists for an individual real estate product known as the neighborhood shopping center, including a profile of neighborhood center development and investment firms, an examination of their financial criteria and the fundamental economics of the product, as well as a look at the process in which these firms locate and analyze new opportunities. In addition, the paper provides an overview of theory and practice in retail location analysis, and to what extent developers and investors utilize this sort of analysis. In addition, selected trends in retail consumer behavior, and shopping center tenant mixes are examined with regard to their implications for neighborhood centers.

This thesis has a geographic agenda, in that it focuses exclusively on neighborhood centers in *California* markets. However, many of the issues regarding small centers in California are common to centers throughout the U.S. An examination of California's high population growth, and its effect on demand for small centers is also included.

The paper relies on four general data sources: 1) academic literature on shopping center development and retail site selection, 2) shopping center and retail industry periodicals, 3) financial data from the Urban Land Institute's Dollars & Cents of Shopping Centers, and 4) a survey of investors and developers involved with retail real estate in California. This survey consisted of a questionnaire which was sent to approximately 80 development and investment firms involved with California small centers. The questionnaire dealt with a range of development and investment issues, and attempted to provide a focused look at the development and investment process for California neighborhood centers.

Thesis Supervisor: James McKellar  
Title: Senior Lecturer, Department of Architecture

## **Table of Contents**

A. Abstract.....	2
B. Table of Contents.....	3
C. Conclusions.....	4
1. A Brief Overview of Shopping Center Types.....	8
2. Congestion and the Convenience of Shopping.....	12
3. Retailing Trends and Tenant Mixes.....	17
4. A Brief Overview of Retail Market Research Practices	
a) Theory.....	31
b) Practice.....	38
5. Profile of Firms that Develop and Invest in Neighborhood Centers	
a) Developers.....	44
b) Investors.....	45
6. The Economics of the Neighborhood Center.....	48
7. Funding of New Development and Acquisitions.....	51
8. Planning Issues and the Municipality.....	53
9. The Demographics of California / Conclusions for Investors and Developers.....	55
10. Bibliography.....	60

## **C. Conclusions**

The small unenclosed shopping center has a number of compelling features relative to large regional malls, and developers and investors in small centers should continue to reap the benefits of well located small centers. Existing neighborhood centers, as the smallest of the anchored centers, hold unique opportunities for investors who will benefit from consumer's increasing demands for convenience and accessibility.

In areas in which traffic and congestion are a concern, which include many of California's coastal and near coastal cities and towns, greater shopper convenience can be supplied by tenanting neighborhood centers with national retailers, selling "shopping goods" as well as the "convenience goods" that have made up the traditional neighborhood center tenant mix. In addition, the rise of the two worker household, in California and in the U.S. in general, has constrained the shopping time available to consumers, and thus made convenience a more important aspect of shopping to the majority of consumers.

This demand by consumers for convenience and shopping accessibility, along with the trend of national retailers to locate a greater number of new stores in unenclosed or strip centers, (as opposed to enclosed malls,) has implications for California's

developers of new neighborhood centers. As one of the most rapidly growing states in terms of population, California will need more small centers to supply this growing population with easy access to both its everyday convenience needs, and its more specialized shopping goods. As the California population trend continues its move East and expanding the population of areas further inland, new small center development will be needed.

Financing for new neighborhood centers, while more difficult today with the current retrenchment of small banks and S&Ls' real estate lending, is still available. To some extent, insurance companies, as well as pension funds and their real estate advisors, are filling demand for development funding created by the diminished role of small banks and S&Ls. The pension funds and insurance companies are becoming increasingly more comfortable with financing small centers as long as the tenant base of these centers is weighted toward national chain retailers.

Industry literature and surveys of neighborhood center tenancies indicate that national retailers are becoming a significantly more important part of the small center's retailing mix.

Many sophisticated methods of predicting consumer support for a store or shopping center location have been developed, but

investors and developers are not the primary users of these methods.

While large national retailers do employ these techniques in their store selection process, the small shopping center developers methodology in selecting new sites for centers is done without fully utilizing the many demographic tools available with which the developer might select different regions that seem promising. Instead, it seems largely an intuitive process, in which "hunches" play a large role in the developer's site selection. It is also primarily a local business, in that neighborhood center developers will generally only prospect for sites in areas in which they have area staff.

Anchor tenants are crucial to the success of the neighborhood center, and in a majority of cases developers use these anchors decision of whether or not to locate in their potential site as their "first cut" marketing study.

But while the prospects for unenclosed centers are in general good in California, a caveat for developers of smaller neighborhood centers comes as a result of growing shoppers' demands for not only travel distance convenience, but also for the convenience of having the selection, quality and knowledgeable service afforded by national chain specialty retailers. While these national retailers are becoming increasingly comfortable locating in unenclosed

centers as opposed to malls, *size* of the strip center is important to these retailers, who generally prefer the largest (between 200,000 to 400,000 square feet) unenclosed centers.

Further, the trade area of these national retailers has always been significantly larger than that of the neighborhood center's convenience goods product mix. Thus, the large draw of these national retailers when combined with a supermarket anchor and other convenience goods tenants might stretch the trading area for supermarket shoppers as well, reducing a given trade area's support for a smaller center in favor of a larger one.

## 1. Brief Overview of Shopping Centers:

The shopping center industry and its trade literature have traditionally distinguished between three major types of centers: *neighborhood*, *community* and *regional*.<sup>1</sup> These divisions are based on differences in the type of anchor tenants that locate themselves in centers of each category, the size of the center, and cumulatively, the different overall shopping experience that the different anchors and the varying mix of small shops that typically congregate around these anchors have to offer.<sup>2</sup> These three types represent a spectrum of shopping center sizes and shopping experiences, as opposed to a hard and fast distinction between them; in other words, a large neighborhood center might look very much like a small community center.

However, a significant distinction between these three types of shopping centers that *is* explicit is whether or not a shopping center is *enclosed*. Almost all regional centers are enclosed malls, with a controlled interior pedestrian environment providing access to the small shops and anchor tenants facing this interior "street", as well as centralized egress to the mall's interior shops through both the anchor stores and central entrances. Neighborhood and

---

1. An Analysis of Performance Characteristics of Existing Community Shopping Centers in the United States by Kenneth L. Koslow, Masters Thesis, M.I.T., 1988.

2. Ibid, p. 9.



community centers, on the other hand, are open centers, with access to the individual stores and anchors directly from the parking lot. For this reason, neighborhood and community centers are often lumped together in the category of "strip centers", referring to the linear configuration of the anchor and satellite shops. This sometimes creates confusion as this term has in the past been used within the industry to describe a small grouping of *unanchored* retailers within one linear commercial building. The Urban Land Institute (ULI) has attempted to clear up the confusion by distinguishing between unanchored *strip commercial* development, and the anchored *strip shopping center*.<sup>3</sup>

All three of these major types of centers have as a common characteristic a tenant mix of *anchor* stores providing the basic "draw" to shoppers, surrounded by *satellite* or *small shop* tenants, which provide some complementary good or service to the anchor's goods. The basic premise of the shopping center is the *synergy* that is created when the proven draw of an anchor, (such as grocery store, a national discount department store, a full-line department store, etc.) is teamed with the convenience and variety of the surrounding small shops. Thus, in one stop, the shopper can accomplish a variety of shopping tasks, after being drawn to the center by the anchor's shopping activity. The unanchored strip centers mentioned above do not function in this way, and while

---

<sup>3</sup>. Ibid, p.13.

these centers can be profitable, the markets for these types of centers are fundamentally different from those for anchored shopping centers.

The neighborhood center, the smallest of the three center types, provides convenience goods and personal services; in other words, items for daily living needs.<sup>4</sup> The neighborhood center is typically anchored by a supermarket and a large drugstore, with small shop tenants consisting of dry cleaners, liquor stores, frozen yogurt/ice cream stores, shoe stores, video rental, etc. The majority of the centers customers for these everyday goods will typically reside within a 6 minute drive from the center, although in certain locations this trade area can be anywhere from 6 to 10 minutes driving-time from the site.<sup>5</sup> Typically, these centers range from 40,000 to 110,000 square feet of Gross Leasable Area (GLA). The median size of the 315 centers located throughout the U.S. was 66,328 GLA, as surveyed by the Urban Land Institute in 1987.<sup>6</sup>

The community center generally offers the same sort of anchor convenience items, such as a supermarket and a large drug store, but adds a wider range of retailer types, such as a junior department store, a large hardware/appliance discounter, a

---

4. Dollars and Cents of Shopping Centers : 1987 published by the Urban Land Institute, Washington, D.C., 1987.

5. Shopping Centre Development by John Dawson, Longman, Ltd., New York, 1983, p.76.

6. Op.Cit., ULI Dollars and Cents...1987, p.170.

furniture retailer and soft lines, such as men and women's clothing. In the last few years, community centers have been anchored increasingly by specialty stores (such as a furniture warehouse, a large home improvement store or a general merchandize discount store such as Wal-Mart or K-Mart) and to a lesser extent by junior department stores. Of the ULI's 262 surveyed centers of 1987, the median size was 151,015 GLA, with an approximate range from 92,000 to 250,000 GLA.<sup>7</sup>

A related off-shoot of the community center that has been gaining popularity in the past 4 four years, and is beginning to qualify as separate center type in its own right, is the "*power center*." This is a center comparable in size to a community center but usually larger (approximately 175,000 to 400,000 square feet of GLA) with a tenancy made up almost entirely of national specialty retailers. Each of these retailers are high visibility, nationally recognized merchants that rely heavily on advertising to achieve high-volume sales. These "category killers" as they are called in the industry could each conceivably serve as one of the anchors of a community center; in a power center, many of these retailers are brought together in the interest of creating a synergy that increases the drawing power of the center.<sup>8</sup>

---

7. Ibid., p.115.

8. Op. Cit., Koslow, p.14.

Finally, the regional center offers a wide range of general merchandise, comparable to the mix found in the central business district of a small city,<sup>9</sup> such as apparel, home furnishings, furniture, as well as a range of prepared food and services supplied by the local satellite tenants. Satellite tenants at the regional center are also often national retailers as well, supplying various shopping goods, (as distinct from convenience goods. See Section 3, *"Retailing Trends and Tenant Mixes."*)

The typical regional mall is built around one or two full-line department store anchor tenants, each of which is generally 100,000 square feet or more.

## **2. Congestion and the Convenience of Shopping**

These different types of centers (and individual retail establishments) and the different product mix and quality of shopping experiences they offer demonstrate a hierarchy of trade area sizes; in other words, the *trade area*, or area from which the majority of the individual center's customers reside, will vary by type of shopping center. The chart below shows a range of retail establishments, (all Supermarkets) and shopping centers, and the

---

<sup>9</sup>. Op. Cit., ULI Dollars and Cents...1987, p.68.

size and the percentage of total sales represented by those residing within a mile of the site:<sup>10</sup>

Type	Location	Primary Trading Area Size (Radial Dimension)	% of Total Sales in Mile Area
Neighborhood	Freestanding Supermarket	1/2 to 3/4 mile	65% to 70%
Central Business District	Supermarket	1/2 to 3/4 mile	70% to 75%
Neighborhood Business District	Supermarket	3/4 to 1 mile	60% to 65%
Neighborhood Shopping Center	Secondary Business District	3/4 to 1 mile	60% to 65%
Supermarket		1 to 1 1/4 miles	60% to 65%
Highway Business Strip		1 to 1 1/4 miles	55% to 60%
Highway Freestanding		1 to 2 miles	40% to 45%
Edge of Downtown		1 1/2 to 2 miles	50% to 55%
Community Shopping Center		1 1/2 to 2 miles	50% to 55%
Regional Shopping Center		1 1/2 to 2 1/2 miles	35% to 40%

Note that the data in this chart was compiled in 1966; given the proliferation of small centers that has occurred since then, plus the general demand for greater convenience from two income families, it seems reasonable to assume that the primary trade area for a typical neighborhood center has become smaller than those reflected in the figures above. In other words, that *more* than 60% to 65% of an anchor supermarket's customers reside within a mile of the site.

---

10. A Systematic Guide to Supermarket Location Analysis by Bernard J. Kane, Jr., Fairchild Publications, Inc., NY, 1966, p.92.

This concept of a shrinking trade area is especially relevant in high population growth areas of the country. As populations expand regionally, and as traffic and congestion become increasingly significant, what once was a 6 minute drive to the large neighborhood center for groceries becomes 10 minutes, then 15. For the last 10 years, California has experienced 22.2% population growth, among the highest in the nation.

This growth rate is projected to moderate, but still remain high relative to the rest of U.S. throughout the '90's.<sup>11</sup> In particular counties and census blocks, growth in California has more than doubled this state-wide average. Given that convenience of traveling time is viewed as a major factor by retail analysts in a consumer's decision process of whether or not to shop at a given location, more homes and greater congestion point to the continued demand for more neighborhood centers, with smaller trade areas to reflect these increased driving times.

As an example of the effect of congestion on driving times, 10 years ago in the City of Costa Mesa of Orange County, California, located a short drive from the coast, a six minute drive covered over over 4 miles. Today, that same six minute drive in average

---

<sup>11</sup>. Regional Economic Growth in the United States: Projections for 1988-2010 by Nestor E. Terleckyj and Charles D. Coleman. NPA Data Services, Inc., Washington, D.C., 1988, p.6.

traffic covers only 2.5 miles, and significantly less in morning and evening traffic. Rapid population growth and infrastructure that has not kept pace with this growth has meant greater congestion, and greater difficulty of travel for many areas of California.

Population growth, as opposed to income growth, is especially relevant to demand for neighborhood centers; since the product mix is mainly convenience goods such as groceries and personal care/drugs, spending at a neighborhood center is considered more "recession proof" than other types of retail in that the majority of the neighborhood center items are not discretionary purchases.

The two-worker household, as noted above, is another reason consumers are placing a higher priority on convenience of shopping. As the nation becomes characterized by two worker households, the time available to the household for shopping activities becomes more constrained; as a result, convenience of shopping becomes more attractive.<sup>12</sup>

The consensus of many in the shopping center industry seems to be that this convenience is best supplied by strip retail, ie: non-enclosed shopping centers such as the neighborhood or community center. The ability to see an individual store's facade from one's car, and the ability to park nearby it, as well as the

---

12. Shopping Center Development and Investment by M.A. Hines. John Wiley & Sons, New York, p.48..

ability to scan the other shopping opportunities at a glance, makes unenclosed centers increasingly popular with shoppers who are time-constrained. One neighborhood center developer pointed to changing demographics as an additional factor in some consumers' preference for strip centers over enclosed malls.

"...People's lifestyles are changing in ways that make them more disposed to shop at the new style of strip centers rather than at malls. About 70% of married women now work outside the home. They do not have the luxury of shopping at the mall a couple of times a week. Whatever time they have must be used very efficiently. The ability to get in, get out and get what they need is very important. That is something strip centers offer that malls just can't."<sup>13</sup>

The CEO of a Pittsburgh-based community center developer echoed this perception of open centers providing greater convenience:

"With both parents working and single parent households, time is very critical. Not to say that large regional malls aren't viable. They are viable, but there are only a few of them. Most women want quick, convenient shopping, which can be found in a strip center."<sup>14</sup>

---

13. Shopping Center World, November, 1989, p.248.

14. Ira Gumberg, CEO of J.J. Gumberg Company, interviewed in Shopping Center World, November, 1989, p.250.



### 3. Retailing Trends and Tenant Mixes:

It's important to make the distinction between *leisure* shopping and *destination* shopping. Leisure shopping involves the consumer's being attracted to a center not simply for the goods available there, but also for the entertainment value of walking around. The regional center has traditionally been a place for both types of shopping; the anchors provide the destination, and the satellite shops provide more interest for those who enjoy "cruising the mall."

On the other hand, destination shopping takes place when a consumers' shopping trip is motivated by a desire for a specific good, service or store. There might also be an element of recreation in this shopping experience as well, but the primary motivation is in the store or the thing itself.

Another way of distinguishing between two different shopping experiences is by the product or service. Retailing and site selection literature traditionally distinguishes between *shopping* goods and *convenience* goods. For example, furniture is considered a shopping good, as purchases per capita are infrequent, the dollar amounts involved are relatively significant for most, and consequently, most consumers wish to shop in stores that offer a great deal of variety, as well as price competitiveness. Shopping

goods are those goods on which consumers generally spend the most effort in shopping; because value and comparison shopping are important to the purchasers of shopping goods, the trade area for these goods is determined by the availability of these goods in a specific area.

On the other hand, groceries, liquor, personal items, prescription drugs and fast food, as well as some services such as dry-cleaning and barbershop/salons are considered convenience goods, which shoppers buy frequently and in doing so do not require extreme price competitiveness <sup>15</sup> The trade area for convenience goods is determined by proximity to the immediate households, as opposed to the availability and selection in the case of shopping. Convenience and accessibility are more important in determining the trade area of these goods than is size and selection.

The neighborhood center has traditionally provided these convenience goods. However, a trend in retailing over the last few years has been the growing acceptance by national retailers of leasing space in unenclosed community and sometimes even neighborhood centers. Many industry publications point to this trend of national chain stores that had in prior years only been leasing in regional malls now positioning themselves in these

---

15. Geography of Market Centers and Retail Distribution by B. Berry. Prentice Hall, 1967. p.18.

smaller centers.<sup>16</sup> As the chairman of a national strip center development company noted, "Stores that were only going into regional malls before are now realizing that strip and neighborhood centers are an ideal place to sell their wares."<sup>17</sup>

Related to this trend is the rise of specialty discount chain stores, such as Toys "R" Us, Crown Books, and Staples Office Supplies, which sell a limited category of goods, (toys, office supplies) but sell this specialty line in much greater volume, with greater selection and with greater discounts than either department stores or multi-line traditional discount stores, such as Caldor's, Bradlee's or Ames. These are the "category killers" that typically make up the "power center", and this trend toward specialty retailing has a definite consequence for unenclosed centers in general, and more specifically, for neighborhood centers. A retail analyst, in discussing the rise of specialty retailers over discount department stores, characterized the situation:

"In the 50's, (discount chain stores) were structured for housewives, who bought most of the household supplies. Once a week, she drove down in the family station wagon to the general merchandise discount store knowing she could find (a wide range of household products.)

"Today, with everyone pressed for time, family members shop for themselves, and they often head out for one particular

---

16 Chain Store Age Executive, November, 1987, p. 72.

17. Irv Maizlish of Leo Eisenberg Company, interviewed in Chain Store Age Executive, "Small Centers Grow in Numbers and Strength", November, 1987, p.72.

item, not a range of household goods. If they want to buy toys, they go to Toys "R" Us; if they want to buy paper plates for a party, they go to Streamers."<sup>18</sup>

It's important to remember that shoppers do not measure convenience simply in terms of driving-times. The convenience of knowing a national specialty retailer carries certain items and product lines has driven time-constrained consumers to pass by both the traditional discount department store anchors of the community centers, as well as the independent retailers, in favor of "brand name" national retailers, even in cases in which these national retailers are further away than the independents or the discount department stores.

In this way, as national chain stores proliferate, trade areas might be becoming larger, not smaller, for the time-constrained shopper. This has negative implications for the neighborhood center developer who sees his centers as providing convenience goods alone as purveyed by supermarkets and independent retailers. For a class of shoppers increasingly willing to seek out the "brand name" retailers, it seems reasonable that these consumers could combine their grocery shopping with their specialty shopping, and thus reduce the customer base of the traditional (ie: without national retailers) neighborhood centers.

---

18. The Wall Street Journal, "Discount Department Stores Struggle Against Rivals that Strike Aisle by Aisle; Category Killers Take Bite Out of Discount Department Stores", June 19, 1990.

As national chain retailers, which provide name recognition and value, become increasingly comfortable in both power centers and community centers, it is reasonable to assume that *some* of these retailers will also see the advantages of locating in large and well positioned neighborhood centers. In older centers in which land is scarce, the large neighborhood center located close to a residential area could provide the consumer with convenient access to both specialty goods of certain "category killer" retailers, as well as the typical mix of convenience goods such as food and personal items.

For the national specialty retailer, the older and well located neighborhood center (ie: in a relatively densely, already built-out residential area) offers a "quasi-monopoly" on the trade area. In a built-out suburban setting, the development of additional competing convenience oriented retail space is unlikely due to the scarcity of developable land, and the limited dollars available for convenience goods purchases.

Still, a combination such as this of food/convenience with shopping goods, such as televisions and furniture, is sometimes a problematic merchandizing mix, even though it means more convenience to the consumer. Retailing literature points to food shopping and shopper's goods shopping as two separate and distinct shopping experiences for the consumer. The literature is

not entirely sure if there is a synergy in locating, for example, a high volume national brand electronics retailer next to a supermarket. If these two goods represent different shopping experiences and mind-sets, the typical consumer might not avail himself to the convenience of their being grouped together, as a visit to each would require a separate trip: one when he's of a mind to buy groceries, and another when he's ready to buy a VCR.<sup>19</sup>

The three trends of a) national retailers expanding rapidly, b) consumers increasingly preferring national retailers over independents and c) national chains comprising an increasingly significant proportion of small center space, seem clear. Examples of these national retailers include a range of lines from specialty discounters such as Highland's, warehouse clubs such as Price Club, drugstores such as CVS and Pharmor, soft goods retailers such as The Gap and The Limited, and specialty convenience goods retailers such as Streamers, a party goods retailer. The growth of the chains is expected to continue, as time constrained, value and brand conscious shoppers tend toward "brand name" stores they are familiar with, as opposed to the independent "mom & pop" stores.

A consequence of these three trends should be increasing penetration of community and neighborhood centers by the national chains, as well as the continued rise of power centers.

---

19. Adapted from the comments of Bill Wheaton, Lecture in "Real Estate Economics", M.I.T., Spring, 1990.

Along with this prediction that national chains will continue to expand is the consensus among small center developers that the number of viable independent tenants will shrink, and that these "mom & pop" stores will become increasingly difficult to find. Related to this prediction is the consensus view that professional service tenants such as dentists, accountants and lawyers, besides the chain stores, will make up an increasing percentage of the neighborhood and community shopping center tenant mix.<sup>20</sup>

Exhibits 1 through 3 (located on the following pages), trace over time the proportion of national, local and independent tenants in comprising total floor space, total sales and total rents of all ULI surveyed neighborhood centers throughout the United States. The graphs are based on data from ULI's Dollars and Cents of Shopping Centers. Data for regional malls is included in exhibits 4 through 6 to compare and contrast the changing mix of independents and national tenants in the regional malls to the neighborhood centers.

From this national data, it seems that the developer's consensus is valid that a) national and local chain tenants are expanding their presence in neighborhood centers, and b) independent tenants are becoming increasingly less represented in both regional malls and neighborhood centers. Exhibit 1 shows independent tenants percentage of floor space trending down

---

20. Shopping Center World, November, 1989, p.250.

**Tenant Mix by Tenant Type in U.S.  
Neighborhood Centers: Percent of Total  
GLA**

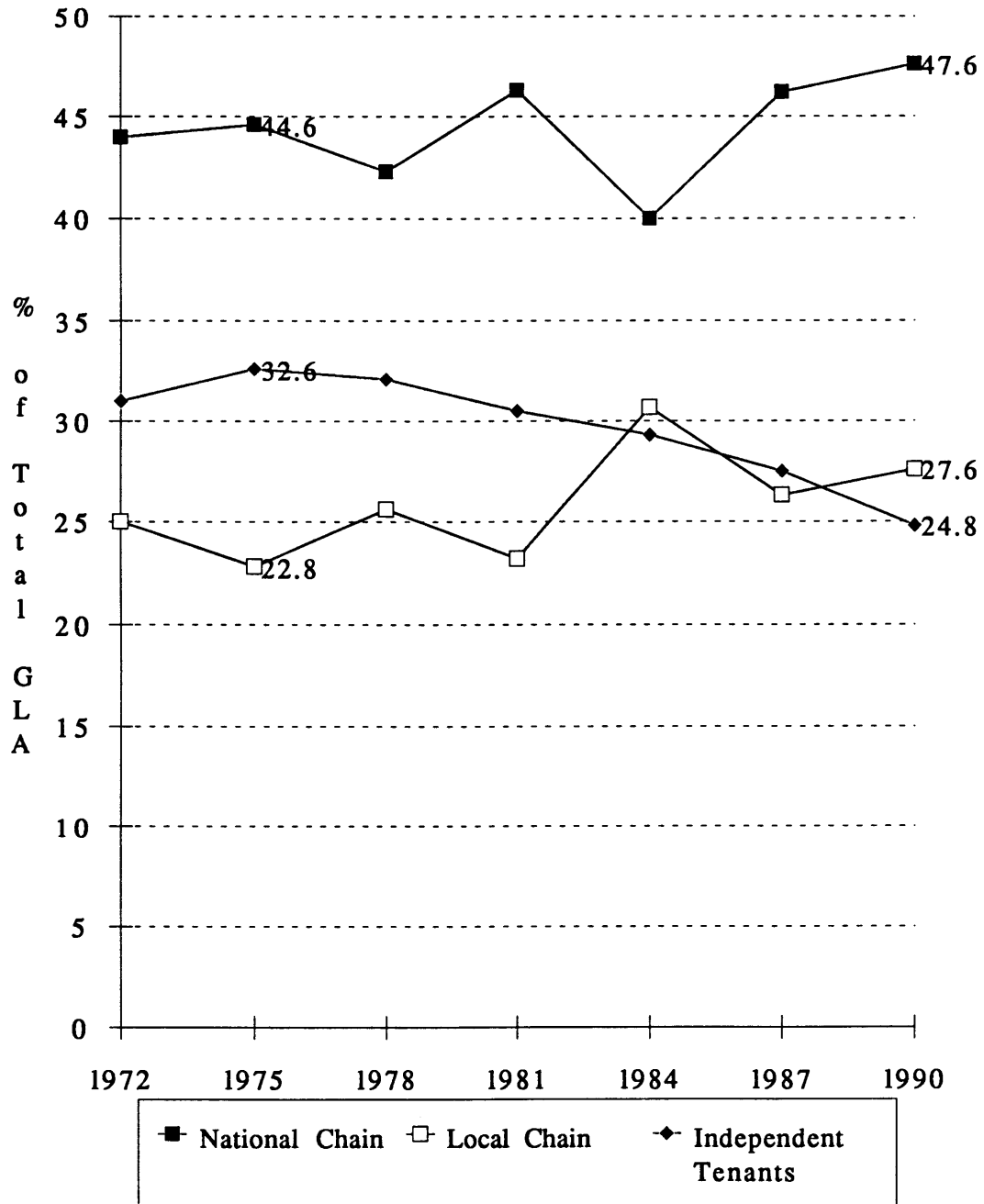




Exhibit 2

Tenant Mix by Tenant Type in U.S.  
Neighborhood Centers : Percent of Total  
Sales

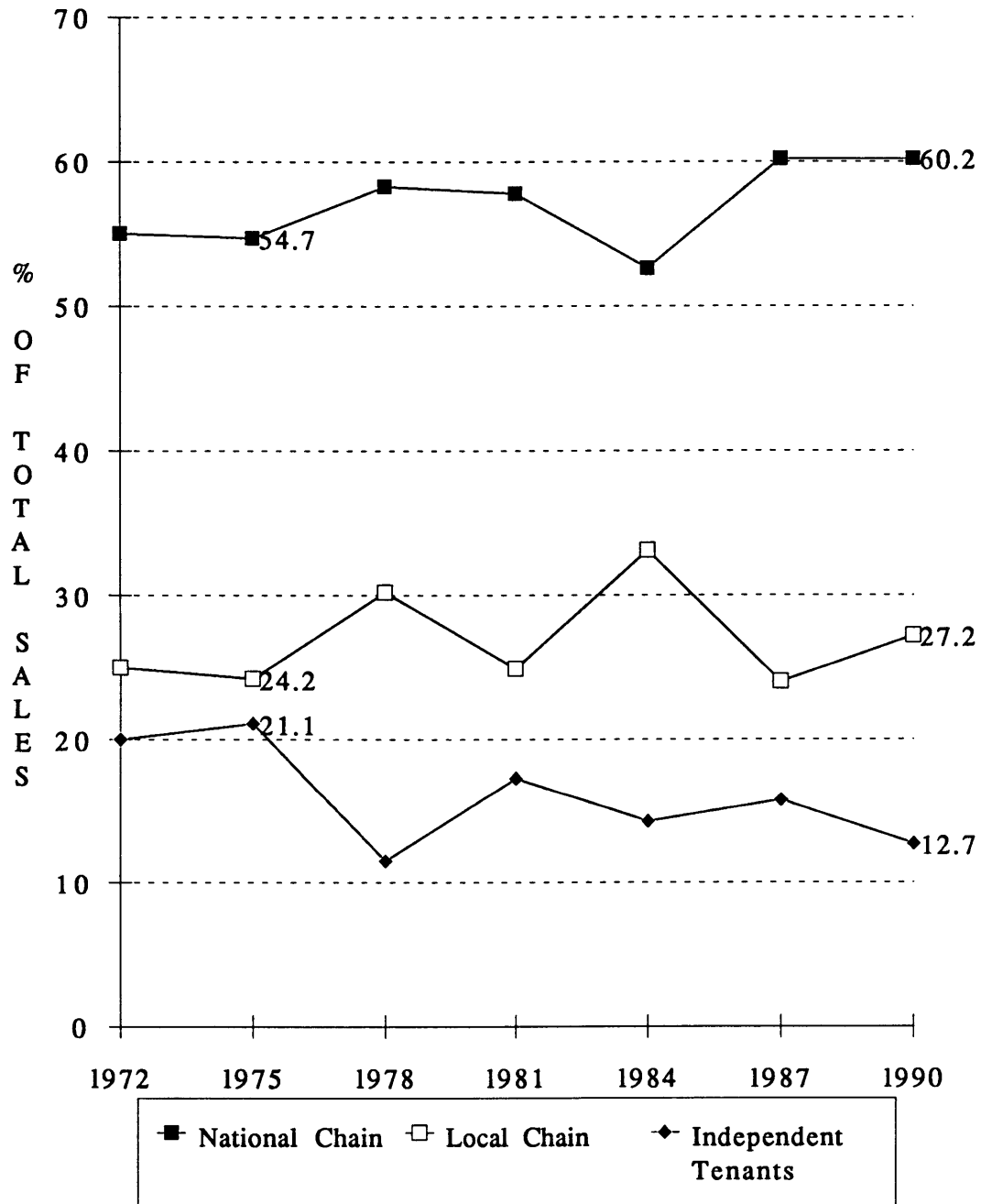


Exhibit 3

**Tenant Mix by Tenant Type in U.S.  
Neighborhood Centers: Percent of Total Rent**

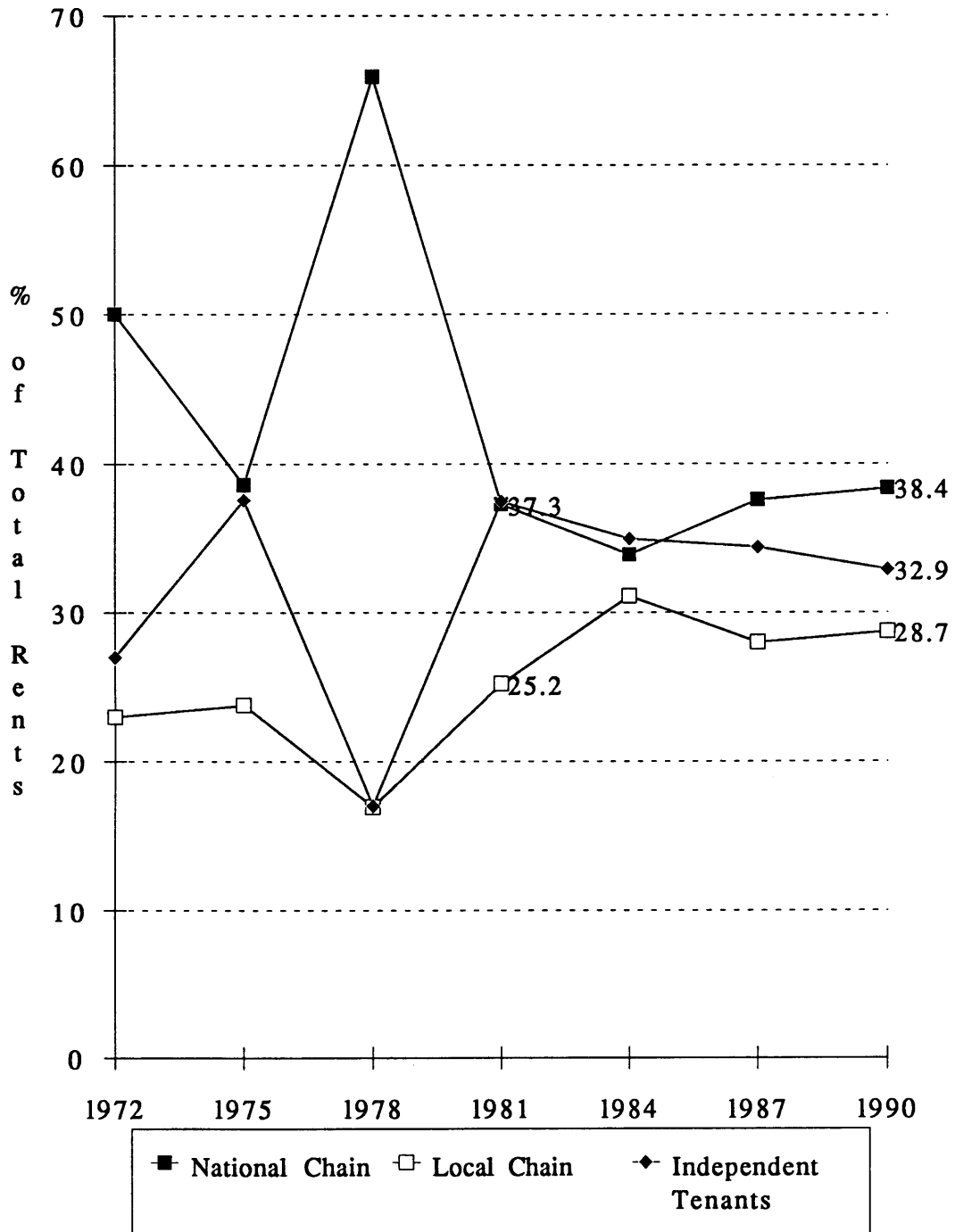


Exhibit 4

Tenant Mix by Tenant Type in all U.S.  
Regional Malls : Percent of Total GLA

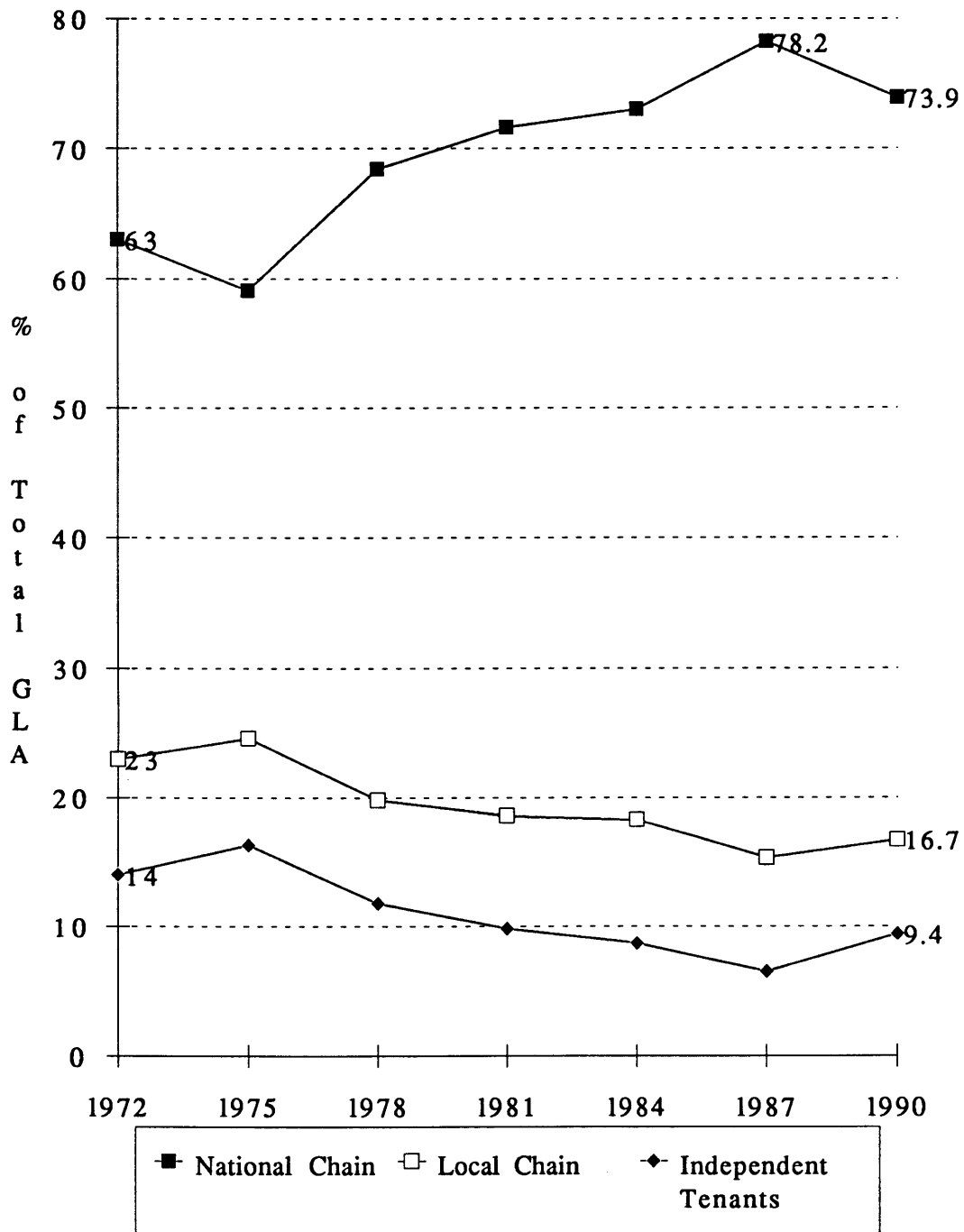


Exhibit 5

Tenant Mix by Tenant Type in U.S.  
Regional Malls : Percent of Total Sales

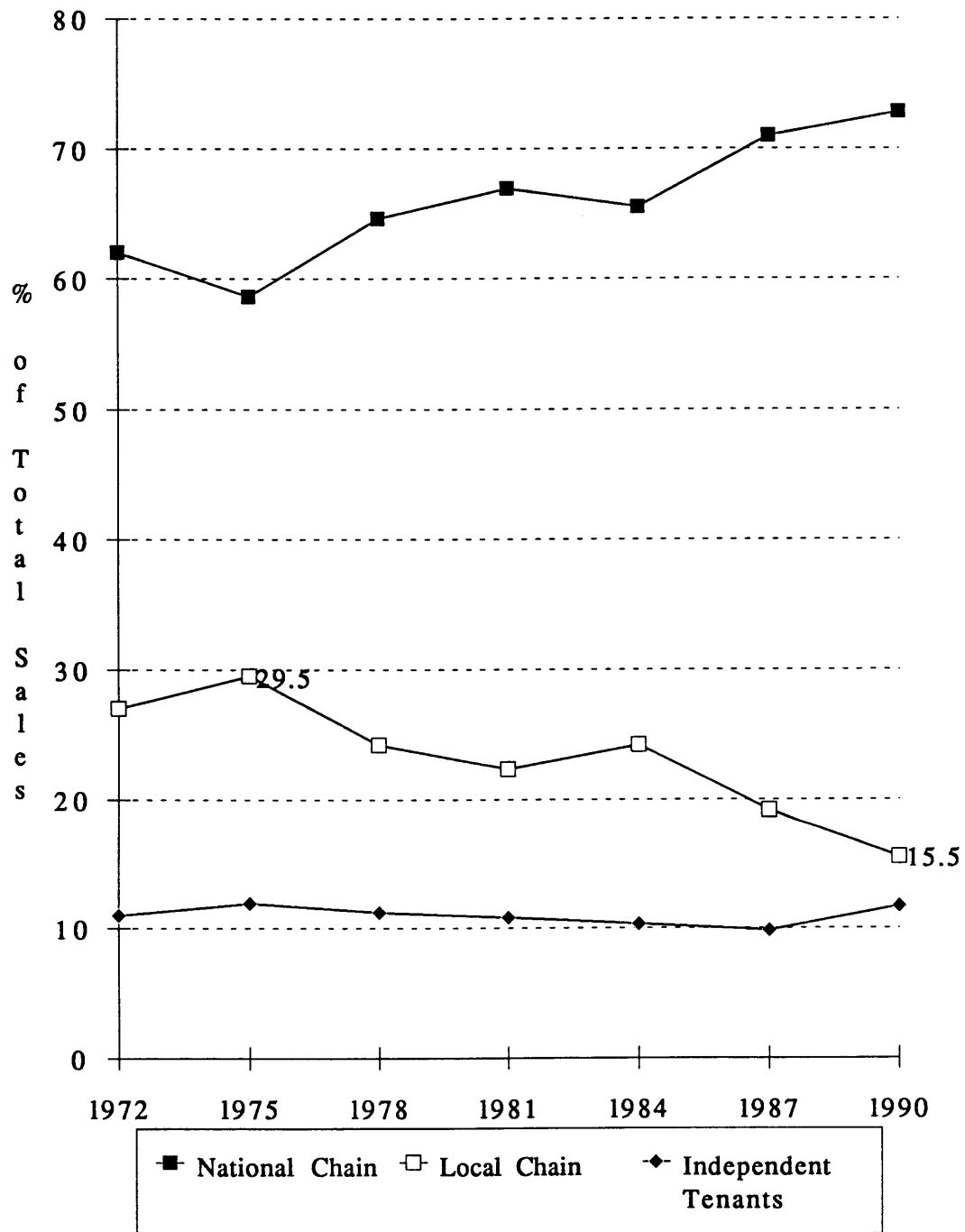
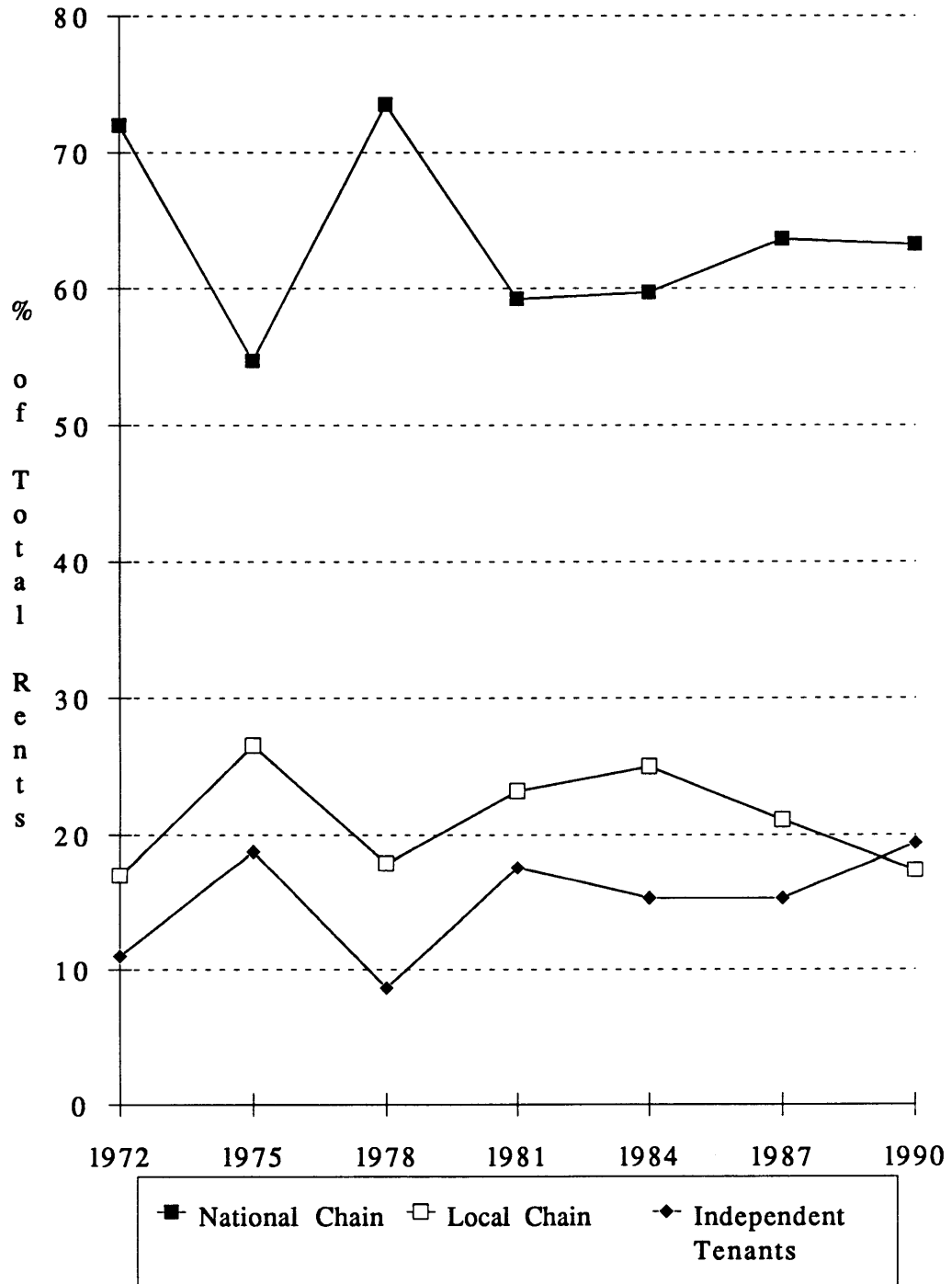


Exhibit 6

**Tenant Mix by Tenant Type in U.S. Regional Malls :  
Percent of Total Rents**



steadily from a high of 32.6% in 1975 to only 24.8% in 1990. Note the slight upward trends of both the local chains and the national tenants in comparison.

The popularity with consumers of both national and local chain stores over independents is supported again in Exhibit 2, in which sales by independents drop from 21.1% in 1975 to 12.7% of total center sales, and national and locals chains' percentages increase from 54.7% to 60.2%, and 24.2% to 27.2% respectively.

Exhibit 3 shows the declining importance of independents in comprising total rents to the center. Ignoring the large swings of the data from 1972 to 1978, independents' percentage of total rents decline from 37.3% in 1981 to 32.9% in 1990. Note how both the local chains and the nationals show a net rise in their percentages over this period.

Exhibit 4 shows the strength of the national tenants expansion programs over the mid-70's and 80's, with national tenants taking up a high of 78.2% of all regional mall space in 1987. The decrease from 1987 to 1990 may be an indication of national tenants turning to smaller centers as a way to continue their store expansions.

Exhibits 5 clearly indicates the growing popularity with consumers of national retailers, with nationals making up a steadily

increasing proportion of total sales, independents holding steady at approximately 10% of total sales, and local chains trending down from a high of 29.5% in 1975 to only 15.5% in 1990.

Exhibit 6 indicates that the proportion of total rents by tenant types for regional malls has been more stable than that of sales, and that while the independents have been accounting for a slightly decreasing proportion of total sales, they have continued to contribute a stable percentage of the malls' total rents.

#### **4. Brief Overview of Retail Market Research Practices**

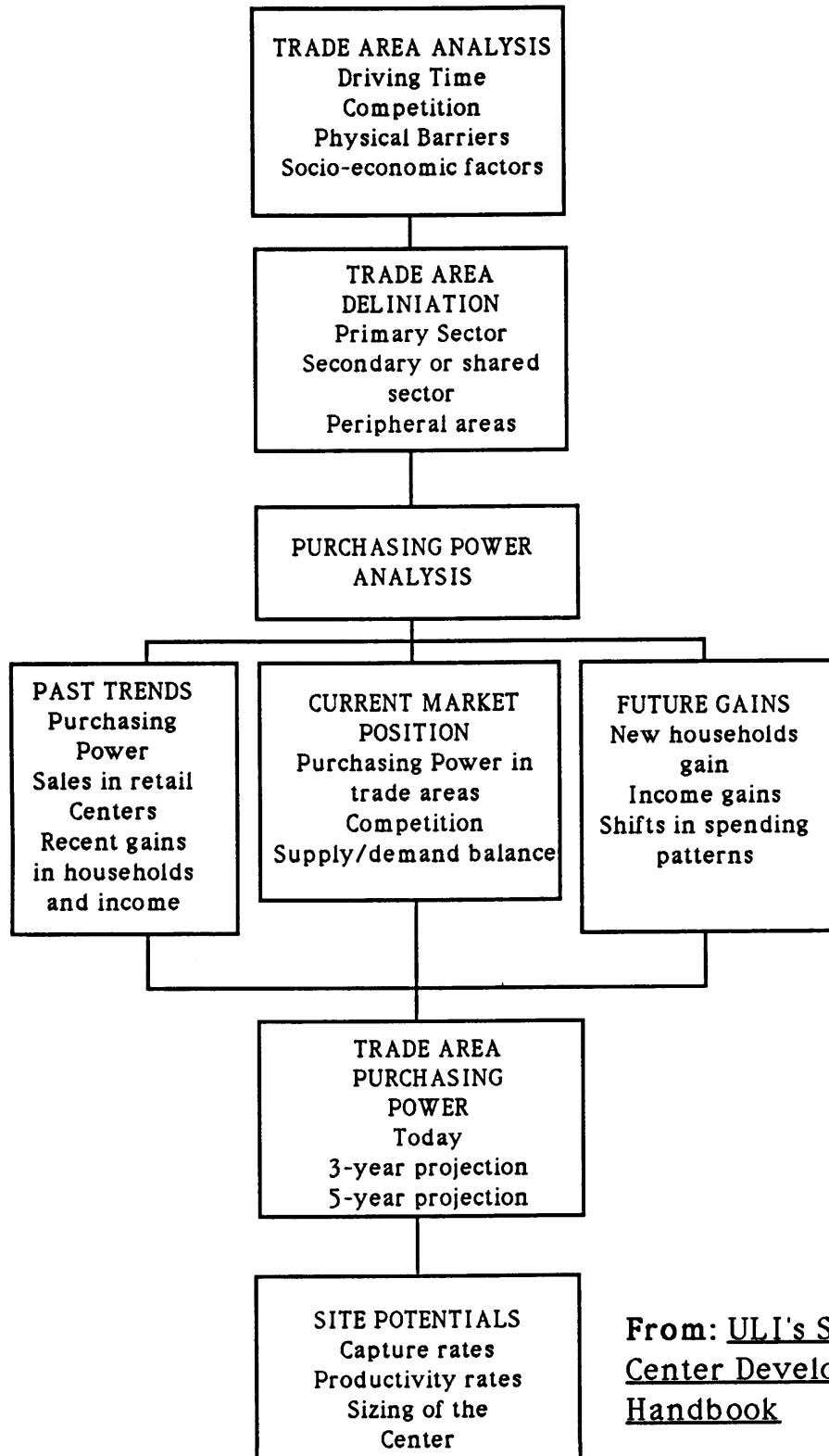
##### **a) Theory**

An entire literature has grown up around the topic of retail market and economic analysis, and the criteria and methodology this literature points to is clearly relevant to the development of neighborhood centers. The basic elements, and the order of a retail market analysis appear in the flowchart in Exhibit 7, found on the following page.

The starting point of the developer's analysis, as defined by most of the literature and exemplified in Exhibit 7, is in understanding a certain *trade area*. A trade area is defined as that area containing those consumers who are likely to purchase a

## Exhibit 7:

### Summary of the trade area assessment procedure in the initial stage of the development process



From: ULI's Shopping  
Center Development  
Handbook



certain type of goods and services from retailers located within a certain travel time from these consumers.<sup>21</sup> As noted before, it is widely accepted among retailers that the trade area for different classes of products varies with the product; for groceries, personal services and other everyday items, the accepted trade area size is an area delineated by a 6 to 10 minute driving radius from the location of the retailer. In other words, a typical person can reasonably be expected to drive six to ten minutes from home to market for this type of shopping experience.

Understanding what constitutes the trade area of a certain location relies on the analyst's assessment of the driving time from outlying areas to a particular site, the placement of competing stores within this drive time radius, and the physical barriers such as lakes, parks, rivers that separate different areas, and make travel time between two points greater than an acceptable time for convenience shopping.

Practice among market analysts in looking at trade areas for supermarket site selection has been to define primary, secondary and tertiary trade areas as part of an overall trade area, with the

---

<sup>21</sup>. Shopping Center Development Handbook, published by the Urban Land Institute, Washington, D.C., 1977, p.3.

primary trading area being defined as that residential area from which between 65 to 85% of all sales originate.<sup>22</sup>

Basic to most retail market analysis is the use of the *central place theory*, a body of theory developed by marketing geographers to account for the regularity in the marketing functions performed by the central places of the areas served. This theory deals with consumer and business behavior, and attempts to outline a rationale for how and why consumers shop in certain geographical patterns, and why certain locations tend to become more intensely utilized clusters of retail and other commercial activity.<sup>23</sup>

Related to this theory is the concept of centrality, which holds that consumers will gravitate toward those retail centers at which they can conduct their shopping with a minimum of effort. The more frequent the shopping, (ie: for items such as convenience goods), the more cumulative "effort" is required, effort being defined generally as travel time. For frequent shopping, then, the theory of centrality holds that the shopper will seek to minimize the aggregate effort expended on, for example, food shopping, by placing a premium on accessibility to the retailer.

---

22. A Systematic Guide to Supermarket Location Analysis by Bernard J. Kane, Jr., Fairchild Publications, Inc., NY, 1966, p. 32.

23. Guide to Store Location Research, edited by William Applebaum, Addison-Wesley Publishers, Reading, MA, 1968, p.14.

When shopping for shopping goods, on the other hand, the consumer will also seek to expend as little effort as possible, but the lesser number of trips for shopping goods relative to convenience goods, and the shopper's desire for value conscious shopping when buying shopping goods will cause the shopper to put *less* of a premium on accessibility, and more on price, size, selection, etc. This theory of centrality provides a rationale for why the trade area for a supermarket-anchored neighborhood center is much smaller than that of a super-regional mall.

A technique known as a gravity model, based on the work of retail analyst William J. Reilly in 1929 and related to this theory of centrality, is still employed by the market research firms and major supermarket (and drug chain) retailers as a means of assessing a trade area for a certain geographical region. Simply, the gravity model takes as its rationale the law of gravity, in asserting that the attractiveness of a retail location (ie: its "gravitational drawing power") is a function of its size and attributes (ie: its "mass") and its distance from other competitors (ie: its position relative to other bodies which have their own gravitational drawing power.)

Theoretically, to find the point that separates the trade areas of two stores, (ie: the point at which the probability a resident will go to one store as opposed to its closest competitor is 50%,) Reilly's law of Retail Gravitation equates this trade area boundary to a

function of distance between stores and "mass", or store size and amenity level.<sup>24</sup> In using a technique such as this, a retail analyst is able to assess trade area boundaries.

Note that in using the Gravity Model, a trade area isn't simply defined by a certain driving distance to the store or center location based on the type of goods and services being offered, but takes the immediate competition into account by both distance and quality level (including size.) The net result of using a Gravity Model is to define a trade area that accounts for the majority percentage of a store or center's potential trade with greater accuracy than by simply drawing drive-time radii around a center site.

In addition to defining a trade area for a potential site based on residents within this trade area, another source of consumer support that is generally considered by a retail analyst is "stop-off" business, ie: trade that results from customers who don't live within a trade area stopping off at a site that is along side a traffic route. (Stop-off business is vital to the success of convenience food stores, such as 7-11's, as well as fast-food restaurants.<sup>25</sup>) However, in the case of the supermarket and the neighborhood center built around it, past studies have found that the significant majority of

---

24. Handbook for Real Estate Market Analysis by John Clapp, Prentice-Hall, New Jersey, 1987. P.41-43.

25. Ibid., p.60.

customers reside within a 6 minute drive-time of the site, and that stop-off business isn't significant.

The major question for the retail analyst that remains once the trade area is mapped out is whether this area contains enough consumers with enough disposable income to support the planned retail establishment. This brings the analysis to the the "Purchasing Power Analysis" section of Exhibit 7.

Census data on population and income levels by narrowly defined areas (such as the census tract, a unit of area which commonly contains approximately 4000 individuals) is used by the analyst to understand the population of a defined trade area as it exists today. Projections of future population and/or income gains are generally made based on both Census Bureau forecasts as well as local chamber of commerce forecasts.

A technique for assessing whether a trade area contains enough income to support another neighborhood center is known as *gap analysis*, which compares supply and demand of retailing facilities in the market area to determine whether the trade area is adequately or inadequately supplied. This technique is related to the gravity model, in that as its starting point it attempts to define a reasonable trade area for the new site in much the same way the gravity model does.

Once this area is defined, and the basic income levels of the area residents is determined from the census data, typical per capita spending levels from the Census of Retail Trade for the products in question (in this case groceries and other convenience goods) are compared to a typical sales per square foot of retail space, multiplied by the retail space within the trade area. In this way, gap analysis attempts to compare the dollars that existing convenience goods retailers are taking in with the dollars that the trade area has available to spend on these items.<sup>26</sup>

When an analysis of this kind shows that income available is greater than total sales at the existing retail facilities, it generally indicates that the trade area could support more retail space, and that a portion of the areas available convenience food dollars are "leaking" into other trade areas.<sup>27</sup>

#### **b)Practice**

It is interesting that the starting point of the majority of the market analysis literature is the specific site, which is analyzed as to its trade area characteristics. Given that population and per capita income comprise such an important part of the analysis, it might seem that these factors alone might be used as a guide to determining which geographic regions (on a town or county level) a

---

<sup>26</sup>. Ibid., p.168.

<sup>27</sup>. Chain Store Age Executive, February 1988, p. 14a

shopping center developer might want to investigate further. With the rise of increasingly detailed and easily accessed demographic databases, and the importance of this information to the success of a retail development, it would seem likely that neighborhood center developers would use these databases extensively as a guide to new markets.

In practice, this is not the case. The California developers and investors surveyed were asked if they felt they could use available demographic information, including forecasts for growth, as guide to locating in specific counties or towns. Almost all viewed the site selection process as a fundamentally "bottom-up" process, in which the real in-depth market analysis begins to take place once a certain site has been identified.

The large majority of those surveyed felt that their own company's general knowledge of a particular town or county was sufficient to begin the process of targeting a particular area, such as an intersection of major roads, for purchase or option. The development process, according to these developers, never began with demographic report, but rather, with their own "gut feelings" for a town and a specific site. As one developer put it, "You know by experience where the growth is going to be; you don't need a market study to tell you where to go."<sup>28</sup>

---

28. Telephone interview with medium-sized Riverside County (CA) developer, June, 1990.

Rules of thumb were popular with many of the developers in assessing the adequacy of an areas population to support a neighborhood center. However, these rules of thumb varied widely by development company, and reflected the firms' different risk criteria; while one firm looked for at least 35,000 people within a three mile radius of the site, another firm wanted 25,000 to 30,000 people within *one* mile of the site! While most of the firms did use general rules of thumb such as these, all of the individuals interviewed made it clear that each situation was different, and that rarely could one individual figure "make or break" a deal.

But while the developers did not use demographic tools to initially focus on a particular area, once a site had been identified, most of the surveyed developers and investors used private demographic information firms, such as Donnally Marketing Information Services, (a subsidiary of Dun & Bradstreet Corporation) or CACI, Inc. of Fairfax, VA, as a tool for making a "first cut" initial evaluation. These firms maintain databases of census population and income data which allow development and investment firms to quickly and inexpensively determine the population and purchasing power of a particular area.

One problem with the way in which the surveyed real estate firms *used* these demographic services was the fact that trade areas were not reasonably defined in relation to a particular site. Standard practice among the market research firms and the



developers and investors who use their services is to define the trade area of their potential site as circular area between 1 and 3 miles in radius with their site at the center. The problem with this "bull's-eye" trade area is that it doesn't make reference to either the area competition or the geographic boundaries such as interstates or public parks and cemeteries that effect the travel time of various regions within this bull's-eye. Therefore, it presents an inflated picture of its actual trade area.

In other words, many developers are satisfied with a view of a trade area that is somewhat arbitrary and incomplete. However, in a real sense they don't have a choice, in that there isn't a simple method for using a rudimentary gravity model to take the competition into account in defining a trade area. therefore, developers continue to use a bull's-eye.

It should be noted that while retail market research is sometimes a cursory affair for the small center developer, the supermarket and drug store chains are widely regarded within the retailing field as the most rational and calculated market researchers. Extensive in-house data bases and on-staff research staffs for identifying macro regions to target for expansion, as well as complicated computerized gravity models to seek out sites on a micro level, help make these firms successful in their site selection and analysis.

Therefore, it's no surprise that many developers will use the initial commitment of one of these anchors as the validation of his choice of the site. The overwhelming response by the surveyed developers to the question of what criteria they used in evaluating a site was the acceptance of the site by the potential anchor tenant: "We piggy-back on the anchor's research." "The first thing we do when looking at a piece of property is show it to the anchors...Generally, we don't see any market studies unless the retailer shows us what he's put together." "We don't get too heavy into the market research; if the anchors like it, we know we've got a winner."<sup>29</sup>

As the typical land purchase for a retail site is so full of contingencies and escape clauses, the firm's interviewed described their "90 day free-look" as the time they used to solicit interest in these anchor tenants. Other than the time and effort to negotiate the option or purchase agreement, the development company is rarely at risk in tying up a sight while soliciting interest in the anchors because of this free-look period.

In many of the firms interviewed, the supermarket chain itself has initiated the development process by directing the development company to a certain town or even a certain intersection. The supermarket's in-house store location staff

---

29. Selected questionnaire responses of 3 medium-sized Los Angeles County retail developers, June, 1990.

determines a location or area in which they wish to expand, and the chain asks the developer to come up with a site at a viable price within this proscribed area. The relationship built up between the tenant and the development firm from past deals is generally the foundation for the chain to initiate this sort of deal.

In this way, the supermarket's store location staff is able to choose an area they want to be in, without the difficulties of developing the site in-house. Usually only a single development firm is contacted to begin investigating a certain area, as opening up a certain site to more than one firm would have the side effect of raising the price of land as development firms attempt to outbid each other.

In the case of the developer who has *not* been directed to a site by an anchor tenant, the developer generally must put together a simple "package" of demographic information and projections with which to arouse initial interest in the anchor tenants he first approaches.

## **5. Profile of Firms that Build and Invest in Neighborhood Centers**

### **•Developers**

While major retailing firms occasionally drive the growth of individual new centers, (ie: a supermarket chain developing a center on its own in an area in which it wishes to establish a presence) the majority of centers are developed by private development firms. Of these firms, industry wisdom has always held that as the smallest (relative to regional and community centers) type of center, the smaller, sometimes undercapitalized entrepreneur has naturally gravitated to this product. While this may be so, interviews with many of the the largest retail firms made clear the fact that these firms as well are involved in the development of neighborhood centers. Companies that develop large enclosed malls in many cases have divisions that develop community, neighborhood and power centers.

Public firms such as Weingarten Realty Investors, a Houston-based Real Estate Investment Trust, develops and holds centers exclusively in the 100,000 to 300,000 square foot range, the majority of which are anchored by supermarkets and drugstores.<sup>30</sup>

---

30. Forbes, July 24, 1989, p.43.

Clearly, large and well capitalized players are a force in the neighborhood center business.

### **•Investors**

The trend in who invests in unenclosed centers has continued to move from wealthy individuals toward institutions. Fifteen years ago, community centers were being developed and held almost exclusively by smaller development companies, with a market being made by individual real estate investors. Insurance companies completed the market in taking equity positions in new center ventures through participating mortgages.

Today, an increasing number of pension funds and their realty advisors are investing in community and power centers.<sup>31</sup> Whereas 10 years ago most institutional investors remained high up the "quality ladder," staying predominantly in regional and super regional mall investments, now many of the major funds are investing in neighborhood and community centers as well.<sup>32</sup>

Neighborhood Centers remain problematic for the institutional investor, however, as the smaller size of the center relative to the power and community centers makes it more

---

31. Interview, Real Estate Investments Manager of a major pension fund realty advisory firm, June 18, 1990.

32. Interview, Major Pension Fund Realty Advisory firm, June 18, 1990.

difficult to manage efficiently. Institutions generally find it more appealing to invest in larger assets that require less time and energy per square foot to manage.

As less regional mall space has come on-line during the late 80's, and as more national retail chain stores continue their expansion, neighborhood and community centers have been able to attract a higher, more credit-worthy tenancy. As institutions are "anchor driven," portfolios of smaller centers with credit-worthy national tenants as anchors are becoming increasingly acceptable to the pension funds.<sup>33</sup>

An investment strategy that has gained popularity with REITs and private firms is the acquisition and renovation of existing neighborhood and community centers in established areas in which new supply is not the issue. Image quality, and the changing demographics of a small trade area, are very important in a renovation strategy, in which centers are repositioned with a more upscale tenant mix that accurately reflects either the increased wealth of a trade area, the sophistication of the shoppers of a specific trade area and their sensitivity to image, or both.

While the basic nature of the center as a convenience goods retailer remains the same, with a supermarket and drugstore

---

33. Interview, Major Industrial Firm's Pension Real Estate Acquisitions Director, June 18, 1990.

anchor, the quality level of the convenience goods satellite shops is boosted, and a mix of slightly more shopping goods, such as national clothing or electronics retailers are added to the tenant mix.

Weingarten Realty Investors has been pursuing an acquisition strategy for centers throughout the Southeast, Southwest and Midwest. By focusing on properties that are "distressed", and yet in Weingarten's view, are fundamentally viable, the company has been able to purchase existing centers for "one half or less" of acquisition cost.<sup>34</sup>

For investors and developers, this issue of replacement cost versus the cost of existing assets is extremely important. Developers who had been making the bulk of their profit through value creation of new centers, (built on affordable land), have found these profits being squeezed by rising land prices in various California markets. Added to the increasingly high cost of land is the problem of potential new supply of smaller centers, in areas in which suburbanization is occurring for the first time.

As a means of addressing both issues, developers and investors have turned to redevelopment of existing small centers, in relatively established areas in which new small center supply is constrained by the residential or commercial development that's

---

34. Forbes, July 24, 1989, p.42.

already taken place. In this sort of environment, the developer or active investor can add value to the project through repositioning and retenanting. both the satellite shops as well as the anchor itself in some cases.

## **6. The Economics of the Neighborhood Center**

The Urban Land Institute regards the capital costs involved in developing the neighborhood center as made up of three components: Land and Land Improvements, Buildings and Equipment and Overhead and Development. Of these three, land cost is the key variable in California, where land price appreciation throughout the 80's has been among the highest in the nation.

The developers surveyed for this paper reported that, for a range of neighborhood centers throughout California, total land costs per square foot of gross leasable area (ie: not the cost of the land itself, but land cost divided by the size of the center) ranged from \$20 to \$35. This reflects the relatively low site coverage of any shopping center, with parking taking up the majority of the site.

Total all-in capital costs for these California developers ranged from \$75 to \$140 per square foot of GLA. Thus, a



hypothetical California center at 76,885 square feet of GLA, (the median area for all neighborhood centers located in the Western states as reported by the ULI<sup>35</sup> using a mid-range figure of \$110/sf of GLA, would cost \$8,457,350. (The ULI compiles figures on national, regional and age groupings of centers. The Western states grouping used by the ULI includes California, Oregon, Washington, Idaho, Nevada, Arizona and Utah)

On the income side, rents vary by wide margins, with the anchor tenants paying least and the independent small shops paying the most. While specific rental data for California centers was not available, the ULI's survey does include a figure for Net Operating Balance (NOB) per square foot of GLA for centers located in the Western states. Net Operating Balance refers to net rental income after all expenses but prior to income tax. For 1987, the median NOB per square foot of GLA was \$5.74.

Comparing net income of \$5.74 to costs of \$110 yields a capitalization rate of 5.2%. ULI also compiles a cap rate figure for its surveyed centers, comparing NOB to capital costs. For all new centers, (defined as those centers between 1 and 3 years old), surveyed throughout the U.S., this cap rate was 6.2%. However, for all surveyed centers located in the Western states of all ages, a cap rate of 15.8% was reported!<sup>36</sup>

---

35. Op. Cit., ULI Dollars & Cents...1987 p.170.

36. Ibid., p.272.

This 15.8% cap rate was significantly the highest of any other geographic grouping surveyed, with the next highest being the Southeast at 10.8%.

The California investors surveyed cited sale prices of existing, recently developed neighborhood centers in popular California markets yielding cap rates ranging from 6% to 9%, depending on the quality of the tenants, the perceived opportunities for retenanting the center with higher paying tenants, and the population and income outlook for the center's location.

The developers surveyed felt that new centers in development needed a 10% to 12% cap rate on development cost in its first stabilized pro forma year to warrant its development. An indication of the popularity of the neighborhood center as an investment product is the differential between the developer's 10% to 12% and the investor's 6% to 8%; Those 2% to 6% points difference indicates the value created by the developer, above and beyond the returns available to the investor.

Similarly, one particular California investment firm's business strategy consists of buying neighborhood centers from their original developer while the center is still under construction, (ie: the anchors are signed up but the satellite shop space has yet to be leased), at a price that yields a cap rate of close to that of the developer's 10% to 12%. The firm then rents the remaining space,

operates and "seasons" the center for a year, and then sells the seasoned, proven center at the typical investor cap rates.

By taking on *some* of the development risk, this firm is able to buy a small center at yields approaching that of the original developer. By selling after a year, the firm realizes the development value it has helped create, and in the process frees up its own capital, and frees itself from the management headaches and operating risks of running a center. One of the firm's principals calls this business strategy, "cap rate arbitrage."<sup>37</sup>

## **7. Funding of New Development and Acquisitions:**

While regional malls have continued to command historically high prices, with cap rates in the most desirable markets at 4.5% to 5.5%, neighborhood centers haven't seen the same sort of price appreciation over the last five years. The reason for this is the fact that it has been institutional investors, most notably pension funds and their advisory firms, that have been bidding up the prices of these regional malls. Pension funds investors are anchor-driven, and up to now, the bulk of small centers' tenants were

---

37. Interview with Partner of Santa Monica-based neighborhood center investment company, at International Council of Shopping Centers Convention, Las Vegas, NV, May 22, 1990.

independents, as opposed to national "credit tenants." The comfort to the institutional investor in any retail development depends to a large extent on the presence of those tenants with a recognizable name and a proven ability to draw shoppers.

Also a problem for large scale investors in owning small centers were the inefficiencies of management in operating a small center relative to a regional mall, as noted in Section 5.

However, one of the trends of the shopping center industry has been the slowing of development of new regional malls in the last five years.<sup>38</sup> Combined with the increasing familiarity of national tenants with smaller centers, it is reasonable to assume that as increasingly attractive national tenants locate in neighborhood and community centers, pension funds will become more comfortable with financing these small centers.

Some pension fund advisors are actively seeking out neighborhood center investments, in the form of participating mortgages. One advisor's deal structure for the participating mortgages it seeks to place for its client funds is a 9 1/4% pay rate, with a 50% share of net cash flow and residual from sale. Moreover, the mortgagee needed to show at least an 11 1/2% internal rate of return at the time of sale. (Compare this return to

---

38. Emerging Trends in Real Estate: 1990 by the Real Estate Research Company, Chicago, IL, 1989, p.23.

the developer's *first year* pro forma returns of 10% to 12% to the mortgagee's return of 11 1/2% *overall* to establish a rough risk/reward range between the two.)

## 8. Planning Issues and the Municipality

An obstacle to new development of neighborhood centers cited by many of the developers who participated in the survey were hostile zoning boards and planning committees. In general, while many land use planners prefer locations for strip commercial to be within residential areas, (eg: infill development), developers prefer sites at intersections of major roads on the edge of residential development.<sup>39</sup> The tension between the two outlooks seems to stem from the planner and the developer's differing views of how the typical American suburb *should* act versus how it *does* act. On the one hand, the developer accepts and caters to a car-oriented consumer, that demands convenient accessibility by car, including adequate parking, for shopping for everyday goods. The planner, however, desires a more pedestrian, urban oriented scheme, in which shopping is immediately accessible to residences, and shopping can take place without car travel, as in a city setting.

---

39. Op. Cit., Dawson, p. 98.

In Great Britain, one finds the majority of centers offering everyday shopping items located within residential areas, due to generally more powerful planning agencies than their American counterparts.<sup>40</sup>

In contrast, many American planning agencies often make land adjacent to residential areas available to neighborhood shopping center use to serve as a buffer between residential and more heavily travelled commercial areas.<sup>41</sup>

The surveyed developers reported that their relationship with the municipality and the planning agency differed widely from town to town. The consensus seemed to be that the closer a municipality was to the Coast, the more stringent its planning agency. Traffic problems and general visual/noise pollution from a commercial use were the most common fears of the California municipalities. The tremendous growth of population in the coastal and near coastal towns over the past two decades has forged a powerful and vocal "no-growth" movement, and these feelings have led municipalities and their planning commissions to view new retail development with extreme skepticism.

---

40. Ibid., p.186.

41. Op. Cit., Hines, p.50.

## **9. The Demographics of California / Conclusions for Investors and Developers**

California has been the third fastest growing state throughout the 80's and is expected to remain so into the 90's. While the United States showed an increase in population of 9.8% from 1980 to 1990, California showed an increase of over 22%. Growth in the 90's for the U.S. is projected to be 7.3%; for California, this population is projected to grow nearly 12%.

Nationwide, the areas with the fastest growth (ie: percentage growth) have typically been smaller Metropolitan Statistical Areas (MSAs), and are located in the South and the West. Of the top 30 fastest growing MSAs, 10 are in Florida, 6 in Texas and five in California.<sup>42</sup>

Clearly, as the most populous state and one of the fastest growing states, California represents significant new retail markets to be served.

Many areas of California are only now beginning to show the magnitude of growth that the areas closer to the coast have been showing for years. In these areas, such as San Bernardino and Riverside Counties, which increased in population by an estimated

---

42. Op. Cit., Terleckyj and Coleman, p.13.

48% and 42% respectively from 1980 to 1990, growth is still a relatively new phenomenon, and continues to be welcomed by these relatively new municipalities hungry for tax revenues. High housing prices, as well as negative area amenities such as smog and traffic congestion, have driven both the outmigration of coastal inhabitants to more affordable inland areas and out of state immigrants to originally settle inland.

Demographers agree that this eastern movement of both the native California population and the effect of immigration from other states to these inland area is significant trend in California's population growth over the last 5 years has been the sustained growth of inland areas. Population growth in these inland areas is projected to comprise an increasingly significant percentage of California's overall growth during the coming decade.<sup>43</sup>

In the more densely populated and congested coastal towns, it will be the *investors* holding existing small centers in these areas who will see the greatest returns as they reposition these centers to provide those residents within these centers' congested trade areas greater product choice and thus, greater ease and convenience of shopping.

---

43. Interview, Western Economic Research Company, Sherman Oaks, CA, July 10, 1990.



California's growing population, in its already densely populated coastal areas and inland, will demand more retailing outlets, and the majority of this retail will be in convenience goods retailers. The demand for ease of access and convenience will mean the continued acceptance of unenclosed centers with a mix of convenience goods tenants *and* national chain retailers.

The growing inland areas will see the greatest opportunities for *developers*. As the trade area for the neighborhood center is the smallest of all types of anchored shopping centers, California's pronounced population growth should have the greatest effect numerically on demand for new neighborhood centers in those areas of inland California that will continue to experience rapid population growth.

However, consumer behavior regarding the preference of national retailers, and the fact that these national retailers generally command larger trade areas, could dampen demand for new centers. If these national retailers locate in centers with a supermarket anchor, and if consumers combine their food and specialty items shopping trips, the trade area of a center with this sort of tenant mix could increase, and thus drive down the number of centers a given area of a given density can support.

The risk exists that trade areas will become larger as shopping goods retailers are increasingly added to the tenant mix

by center developers, and as a result consumers will forego the small center for their convenience goods shopping in favor of larger centers that allow them to do *both* convenience and specialty shopping.

Just as the median size supermarkets and drugstores have been increasing in size over time, it seems conceivable that neighborhood strip centers will have to increase in size to provide the opportunities for national retailers to locate there, and thus provide consumers with the value and "brand name" retailing they seem to be demanding. Developers and investors contemplating a small convenience goods-based center should keep this size factor, given the importance of national retailers to the contemporary strip center's success.

Convenience is becoming increasingly important to consumers, and convenience is comprised not only of short travel times, but also being able to easily select exactly the brand name item for which the shopper left his house in the first place. This is why the national chains have been so effective and shown such steadily rising sales as a percentage of shopping center tenancies: they provide this sort of convenience, and shoppers are increasingly bypassing the independent store with which they are unfamiliar in favor of the chain store whose product lines they *are* familiar with. Again, investors and developers should keep this

very significant trend in consumer behavior in mind when designing tenant mixes.

A crucial question beyond the scope of this paper for investors and developers in California, where land prices are among the highest in the country, is how to build profitable centers with tenancies comprised increasingly of national tenants, who have traditionally paid significantly less rent per square foot of GLA than independents.

## Bibliography

Geography of Market Centers and Retail Distribution by Brian J.L. Berry, University of Chicago, Prentice-Hall, Inc., Englewood Cliffs, NJ, 1967.

Guide to Store Location Research with Emphasis on Super Markets, by William Applebaum, et al, Addison-Wesley Publishing, Reading, MA, 1968.

Handbook for Real Estate Market Analysis by John M. Clapp, Prentice-Hall, Inc., Englewood Cliffs, NJ, 1987.

Market Profiles 1990, published by the Urban Land Institute, Washington, D.C., 1990.

The Owner's and Manager's Market Analysis Workbook by Wayne A. Lemmon, American Management Associations, New York, NY, 1980.

Population Trends in California, published by Western Economic Research Company, Sherman Oaks, CA, 1982.

Project Reference Files (selected), published by the Urban Land Institute, Washington, D.C., annually.

The Real Estate Industry: An Information Sourcebook by Laura A. Harris, Oryx Press, Phoenix, AZ, 1987.

Regional Economic Growth in the United States: Projections for 1988-2010 by Nestor E. Terleckyj and Charles D. Coleman, NPA Data Services, Inc., Washington, D.C., 1988.

Shopping Center Development and Investment. (2nd Edition) by Mary Alice Hines, John Wiley & Sons, New York, NY, 1988.

Shopping Center Development Handbook, published by the Urban Land Institute, Washington, D.C., 1977.

Shopping Centre Development by John A. Dawson, Longman Press, New York, NY, 1983.

Shopping Center Development Guide (Neighborhood Centers) by Curtis T. Bell, published by the National Association of Home Builders, Washington, D.C., 1976.

Shopping Center Strategy by William Applebaum, International Council of Shopping Centers, New York, NY, 1970.

Shopping Center Zoning, published by the Urban Land Institute, Washington, D.C., 1973.

Store Location and Store Assessment Research, edited by R.L. Davies and D.S. Rogers, (DSR Marketing Systems, Deerfield, IL), John Wiley & Sons, New York, NY, 1984.

A Systematic Guide to Supermarket Location Analysis by Bernard J. Kane, Jr., Fairchild Publications, Inc., New York, NY, 1966.

### **Selected Periodicals**

Chain Store Age Executive  
Forbes  
Fortune  
Monitor  
National Real Estate Investor  
Stores  
Wall Street Journal